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IN THE

SUPREME COURT OF THE UNITED STATES.

OCTOBER TERM, 1966.

CHICAGO AND NORTH WESTERN RY. CO. et al., Appellants,
vs.
THE ATCHISON, TOPEKA AND SANTA FE RY. CO. et al., Appellees. } No. 8.

UNITED STATES OF AMERICA and INTERSTATE COMMERCE COMMISSION, Appellants,
vs.
THE ATCHISON, TOPEKA AND SANTA FE RY. CO. et al., Appellees. } No. 23.

On Appeal from the United States District Court for the Southern District of California, Central Division.

BRIEF

For Appellees, Missouri-Kansas-Texas Railroad Company and St. Louis-San Francisco Railway Company.

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INDEX.

	Page
Introductory Statement	1
Questions Presented	2
Statement	3
Summary of Argument	9
Argument	13
I. The District Court Was Plainly Correct in Holding That the Commission Failed to Fulfill Its Lawful Duty When It Refused to Consider the Impact of Its Orders Upon the Katy and the Frisco	13
II. The Katy and the Frisco Did Not Waive Their Right to Consideration of the Fairness of the Prescribed Divisions to Them as Individual Carriers	31
Conclusion	35

Cases Cited.

Akron, C. & Y. R. Co. v. Atchison, T. & S. F. Ry. Co., 316 I. C. C. 351 (1962) 20, 28

Atchison, T. & S. F. Ry. Co. v. United States, 225 F. Supp. 584 (D. Colo. 1964) 10, 20, 21, 28

Baltimore & Ohio R. Co. v. United States, ... U. S. ... (1967) 24

Boston & Maine R. Co. v. United States, 162 F. Supp. 289 (D. Mass. 1958) 24

Carolina & Northwestern Ry. Co. v. United States, 234 F. Supp. 114 (W. D. N. C. 1964), aff'd 380 U. S. 526 (1965) 28

Division of Rates, Official and Southern Territories, 234 I. C. C. 175 (1939) 28

Lehigh Valley Cooperative v. United States, 370 U. S. 76 (1962) 31

Louisville & N. R. Co. v. Southern Railway, 319 I. C. C. 639 (1963) 28

New England Divisions, 261 U. S. 184 (1923)..11, 26, 27, 30

New York v. United States, 331 U. S. 284, 310 (1947) 22

Official-Southern Divisions, 287 I. C. C. 497 (1953)..28

Official-Southern Divisions, 325 I. C. C. 1; 325 I. C. C. 449 (1965) 28, 29

Official-Western Trunk Line Divisions, 269 I. C. C. 765 (1948) 28

Pennsylvania Railroad Company—Merger—New York Central Railroad Company, 327 I. C. C. 475 (1966), 328 I. C. C. 304 (1966) 23, 24

Securities & Exchange Commission v. Chenery Corp., 332 U. S. 194 (1948) 15

United States v. Abilene & Southern R. Co., 265 U. S. 274 (1924) 11, 21-22, 28

Western Pacific Railroad Company Discontinuance of Trains Nos. 17 and 18 Between San Francisco, Calif., and Salt Lake City, Utah, Finance Docket No. 24277, decided February 13, 1967 29

Statutes Cited.

Administrative Procedure Act, Section 8 (b), (5 U. S. C. § 557 (c)) 7
Interstate Commerce Act:
Section 1 (14) (49 U. S. C. § 1 (14)) 24
Section 3 (1) (49 U. S. C. § 3 (1)) 25
Section 5 (2) (49 U. S. C. § 5 (2)) 23
Section 15 (1) (49 U. S. C. § 15 (1)) 25
Section 15 (6) (49 U. S. C. § 15 (6)) 7, 9, 11, 16, 17, 18, 21, 22, 23, 26, 27

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For Appellees, Missouri-Kansas-Texas Railroad Company and St. Louis-San Francisco Railway Company.

INTRODUCTORY STATEMENT.

Appellees Missouri-Kansas-Texas Railroad Company and St. Louis-San Francisco Railway Company (hereinafter referred to as the Katy and the Frisco) fully concur

in each of the arguments of the appellee Mountain-Pacific railroads advanced in the brief which those railroads are filing in these cases. However, the position of the Katy and the Frisco under the Commission's orders is unique, and certain issues raised by appellants are directed almost exclusively at that part of the District Court's decision which dealt with the situation of the Katy and the Frisco. Accordingly, this separate brief is submitted to deal more fully with the issues which arise from the unique position of the Katy and the Frisco.

QUESTIONS PRESENTED.

1. Whether the Commission may lawfully prescribe divisions for a group of railroads without regard to their impact upon individual carriers, where the divisions prescribed cannot be justified under the Commission's group findings with respect to any of the standards of Section 15 (6), and where certain carriers in the group are forced to bear drastic reductions in their revenues, while others receive substantial increases?

2. Whether the Katy and the Frisco waived their right to object to drastic reductions in their divisions by joining other members of the Midwestern group in taking the position that the Midwestern railroads, as a group, were entitled to increased divisions on the basis both of relative cost of service and relative revenue needs?

STATEMENT.

Throughout the hearings before the Interstate Commerce Commission, the Katy and the Frisco were members of the same Midwestern group of railroads as the Midwestern appellants. Together with the Midwestern appellants, the Katy and the Frisco filed a complaint before the Commission seeking increased divisions from transcontinental freight revenues (R. 1-23). This complaint asserted that each of the Midwestern railroads was entitled to a greater part of the transcontinental revenues on the basis both of their proportion of the costs of providing that service and of their greater overall revenue needs (R. 2).

All of the evidence submitted by the Midwestern group of railroads to support this complaint was group evidence, which included data for the ten principal members of that group, including the Frisco and the Katy. The Midwestern railroads' cost study was a group study based upon the average costs of all ten of these railroads (R. 994). The Midwestern railroads' revenue needs evidence was based upon the average rate of return of all ten of these railroads (R. 496, 508). No evidence whatever was introduced before the Commission that dealt with the costs of any of the Midwestern appellants now before this Court separately from the costs of the Katy and the Frisco. And the only revenue needs evidence submitted on an individual railroad basis showed that the rate of return of the Katy was substantially lower than the average rate of return of the Midwestern group, and that the rate of return of the Frisco was somewhat higher (Exhibit MW-221, p. 1; Exhibit MW-734, p. 2).

In its original report, the Commission in no way questioned the inclusion of the Katy and the Frisco in the Midwestern group of railroads. It accepted evidence which

included the Katy and the Frisco as Midwestern railroads, both in its determination of relative cost of service (R. 1009), and its treatment of revenue needs (R. 1023, 1024, 1028). On the basis of this evidence, the Commission found that the Midwestern railroads were receiving a smaller proportion of the transcontinental freight revenues than their proportion of the costs of handling that traffic (R. 1012), and that their earnings prospects in the future, measured by freight income to exclude the effects of differing passenger deficits, "are less promising than those of the defendant transcontinental railroads" (R. 1029). It then proceeded to prescribe new divisions for the Midwestern railroads.

The Commission did not state the extent to which the divisions it prescribed for the Midwestern railroads were supposed to be based upon costs or the extent to which they were supposed to be based upon revenue needs. The only direct statement made by the Commission on this subject would seem to indicate that the Commission leaned most heavily upon revenue needs (R. 1032):

> "From our consideration of the cost evidence previously discussed in this report we are convinced that the present divisions are favorable to the defendants to an extent not justified by ascertainable cost differences. The evidence, however, does not provide an acceptable pattern for readjusting the existing divisions, which must reflect certain broader aspects of revenue need."[1]

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[1] Appellants take the position in this Court that this statement of the basis of the prescribed divisions was directed only toward the divisions prescribed for the Eastern railroads (C&NW Brief, p. 47). However, as shown in the brief of the Mountain-Pacific railroads, this position is inconsistent with numerous statements in, as well as the whole tenor of, the Commission's report, and it is also flatly inconsistent with the position taken by the appellants in the District Court.

However, the divisions actually prescribed by the Commission were not related either to costs or to revenue needs, nor were they explained in terms of these or any other standards of Section 15 (6). The only explanation offered by the Commission for these divisions was that "They would produce moderate increases in some of the most important midwestern divisions" (R. 1039).

The divisions prescribed by the Commission would not produce "moderate increases" in the divisions of the Katy and the Frisco. Quite the contrary, the new divisions would drastically **reduce** their revenues from transcontinental traffic, the reductions being some $132,000 a year in the case of the Katy, and some $423,000 a year in the case of the Frisco (R. 1232, 1233). Such reductions in revenue would have a severe impact upon the financial condition of the Katy and the Frisco. During the five-year period immediately prior to the issuance of the Commission's order, the Katy teetered on the brink of bankruptcy, even under the previous transcontinental divisions (R. 1234):

Statement of Katy Net Railway Operating Revenue and Net Income

Year	Net Railway Operating Revenue	Net Income
1958	$4,438,335	$2,749,571 Deficit
1959	3,781,657	2,985,246 Deficit
1960	3,721,480	3,195,409 Deficit
1961	2,839,250	139,202
1962	2,596,784	12,336

The loss of $132,000 would have left the Katy virtually without net income in 1961 and would have returned it to a substantial deficit position in 1962. The position of the

Frisco is somewhat better, but a loss of $423,000 a year would reduce its net income by upwards of 9 percent (R. 1234).

The effect of the prescribed divisions cannot be calculated from any evidence of record before the Commission, either for the Katy and the Frisco, or for any other Midwestern railroad, or for any group of railroads. Nor did the Commission have available to it the most recent figures shown above with respect to the precarious financial condition of the Katy. Consequently, when the Commission's original report and order were issued, the Katy and the Frisco filed a petition for reconsideration and further hearing at which they offered to prove these facts and to show the Commission that the prescribed divisions could not be justified under any of the standards of Section 15 (6) (R. 1231).

The Commission subsequently issued its supplemental report and order denying the Katy's and the Frisco's petition for reconsideration and refusing to accord them a further hearing (R. 1089-1091). The stated basis for this action was that there is "no reason for making a special exception from our findings for these petitioners" (R. 1091). However, the Commission made no attempt to explain how the divisions which it prescribed were related to its findings with respect to costs and revenue needs, or how those divisions could be justified under any of the standards of Section 15 (6). Instead, the Commission flatly rejected the contention "that the construction of a divisional scale is primarily a matter of costs and mathematics" (R. 1078), and held that this was purely a matter of "judgment" within its discretion (R. 1077):

> "In determining just, reasonable and equitable divisions herein, the process we employed was one of practical judgment and not of mere mathematical computation. We found it impossible to use any ex-

> isting divisional scale, a cost scale, or any method suggested by the parties as an exclusive guide or specific pattern for the divisions to be prescribed. In our view of what the evidence shows as to the equities of the situation, we necessarily had to exercise our judgment . . ."

The Commission did not explain why, in its "judgment", a divisional formula should have been adopted which would reduce the divisions of the Katy and the Frisco even though it also found that the Midwestern railroads, as a group, which included the Katy and the Frisco, were already receiving divisions smaller than their proportion of the costs of handling transcontinental traffic and that their revenue needs were greater than those of the Mountain-Pacific railroads.

The District Court set aside the Commission's orders on the ground, first, that the Commission had failed to make adequate findings with respect to the revenue needs of, and the effect of its orders upon, the contending railroad groups under the requirements of Section 8 (b) of the Administrative Procedure Act (5 U. S. C. § 557 (c)) and Section 15 (6) of the Interstate Commerce Act (49 U. S. C. § 15 (6)). The court went on to deal with the Commission's refusal to consider the fairness of its orders to individual railroads, including the Katy and the Frisco (R. 1726-1729, 1732, 1733). The District Court recognized that under the so-called typical evidence rule, the Commission may base an order prescribing new divisions for a whole group of railroads on "representative evidence relating to particular rates and divisions of particular carriers" (R. 1727). However, the court held that here the Commission had not made sufficient findings on a group basis to satisfy the typical evidence rule. The District Court also held that the typical evidence rule does not operate wholly to excuse a failure on the part of the Commission to consider the situation of

individual railroads, for "the Commission must make sure that the divisions formula under consideration (although seemingly just and equitable when viewed in terms of its impact on a group of railroads as a group) has not been constructed in such a way that its impact on any particular division of any particular rate as applied to any particular carrier is unjust" (R. 1728). The divisional scales prescribed for the Midwestern railroads were therefore held to be unlawful for the additional reason that the Commission had failed to make sure that those scales were constructed so as to produce fair divisions for the Katy and the Frisco.[2]

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[2] Since the decision of the District Court in this case, the Katy and the Frisco have entered into a settlement agreement with the Mountain-Pacific railroads which disposes of the controversy between the Katy and the Frisco and those railroads. However, the divisions of the Katy and Frisco remain in issue on traffic which they handle in conjunction with any of the Midwestern appellants. For example, on a haul from Chicago to Los Angeles via Milwaukee Road to Kansas City and Frisco-Santa Fe beyond, the increased divisions prescribed for the appellant Milwaukee Road are still at issue and the corresponding reduction would be borne by the Frisco and Santa Fe as the carriers west of Kansas City.

SUMMARY OF ARGUMENT.

The basic position of the Katy and the Frisco is that the orders of the Interstate Commerce Commission at issue in this case are unlawful in their impact upon their revenues. The orders in question are supposedly based upon findings of the Commission under Section 15 (6) of the Interstate Commerce Act (49 U. S. C. § 15 (6)), first, that the existing divisions of the Midwestern railroads are less than the proportion of the costs of handling transcontinental traffic borne by those railroads, and, secondly, that the revenue needs of the Midwestern railroads are greater than those of the Mountain-Pacific railroads. These findings were based in turn upon evidence submitted by the Midwestern railroads as a group in which no suggestion was made that the situation of the Katy and the Frisco was any different from that of any other Midwestern railroad. Yet the divisional scales prescribed by the Commission would drastically reduce the revenues of the Katy and the Frisco, while substantially increasing the revenues of other Midwestern railroads which appear before this Court as appellants.

The losses of the Katy and the Frisco result from the fact that the prescribed divisional scales are not related to the findings of the Commission on the statutory standards of relative cost of service and relative revenue needs. Although the Commission sought to explain these scales in terms of the rates being divided, the fact of the matter is that the scales have nothing to do with these rates but are, in effect, drawn out of thin air. Hence, the scales produce divisions for the Midwestern railroads which are wholly unrelated to the standards of Section 15 (6), some railroads receiving substantial increases in their revenues, and the Katy and the Frisco receiving drastic decreases directly contrary to the Commission's findings with respect to their costs and revenue needs.

In view of the wholly unjustified differences in the impact of the prescribed scales, the Katy's and the Frisco's efforts to avoid the application of such scales cannot conceivably be brushed aside as a request for special treatment, as the appellants contend. What the Katy and the Frisco are seeking is **equal** treatment with other Midwestern railroads, or at least some rational explanation as to why they are not entitled to such treatment. To date, they have received neither.

Actually, it is the Midwestern appellants which are seeking special treatment here, although they attempt to obscure this fact by defending the prescribed divisions as producing "moderate increases" for the Midwestern railroads as a group. For even if the prescribed scales do produce "moderate increases" for the whole Midwestern group, the fact remains that the Midwestern appellants must have been given **substantial** increases to offset the fact that the Katy and the Frisco were forced to absorb losses and some other Midwestern railroads would receive approximately the same divisions. The divisions which the eight Midwestern appellants seek to defend thus constitute a windfall to them under their own theory of the case.

Appellants' lengthy discussion of the power of the Commission to prescribe divisions on a group basis and the difficulties inherent in any other approach is largely beside the point. None of the cases cited by the appellants remotely suggests that the Commission can deal with railroads as a group in a divisions case in a way that treats some members of the group quite differently from others. The only time the Commission openly attempted such an action, its order was set aside in a case which appellants now conveniently ignore. **Atchison, T. & S. F. Ry. Co. v. United States**, 225 F. Supp. 584 (D. Colo. 1964). This holding was clearly correct, for both the

express language of Section 15 (6) and the decision of this Court in **United States v. Abilene & Southern R. Co.**, 265 U. S. 274, 291 (1924), require that divisions prescribed by the Commission be fair, not only in terms of their aggregate impact upon railroad groups, but, also, in their impact upon individual carriers.

The cases referred to by the appellants dealing with different statutes regulating other industries in no way impair the authority of the **Abilene & Southern** case. The railroad industry presents unique problems which make it imperative that the Commission consider the impact of its orders upon individual railroads whenever such a course is practical from a competitive standpoint. The only situations in which such consideration is impractical are cases involving the general levels of rates. The divisions-making power was conferred upon the Commission for the express purpose of permitting it to go beyond the limitations of rate cases and deal with the situation of individual railroads. **New England Divisions**, 261 U. S. 184, 189-191 (1923). And the Commission has repeatedly utilized this power for that purpose.

Contrary to the assertions of the appellants, there is nothing either impractical or useless about a requirement that the Commission make certain that the divisions which it prescribes are fair to individual railroads. In the ordinary case, this will require the Commission only to relate its order to the findings upon which it is based so that each division prescribed is justified under the Commission's findings. No separate findings are required unless some carrier asks for special treatment and shows that its situation is basically different from that of other carriers in its group. **New England Divisions**, 261 U. S. 184, 196-197 (1923). The Commission can and should be compelled to meet this requirement, for in no other way can such railroads as the Katy and the Frisco be protected against

wholly arbitrary action, which has no statutory basis, but which can always be defended as fair in its aggregate impact.

The Katy and the Frisco did not waive their right to object to the fairness of the prescribed divisions to them as individual railroads by participating as members of the Midwestern group of railroads in the proceedings before the Commission. The evidence presented to the Commission by the Midwestern group of railroads treated the Katy and the Frisco as wholly typical members of the group with the same right to increased divisions based upon cost of service and revenue needs as any other railroad. The divisional scales proposed by the Midwestern group were an appropriate mechanism for giving effect to the evidence as to costs and revenue needs, at least insofar as the Katy and the Frisco are concerned, and certainly nothing in that proposal indicated a willingness on the part of the Katy and the Frisco to absorb losses in their revenues while other Midwestern railroads received increases based upon cost and revenue needs findings equally applicable to the Katy and the Frisco. If there has been any waiver here, it is on the part of the Midwestern appellants who treated the Katy and the Frisco as typical members of the Midwestern group in the proceedings before the Commission and now, for the first time before this Court, seek to make it appear that the situation of the Katy and the Frisco is basically different from that of other members of the group in order to justify the fact that they were treated differently.

ARGUMENT.

I. The District Court Was Plainly Correct in Holding That the Commission Failed to Fulfill Its Lawful Duty When It Refused to Consider the Impact of Its Orders Upon the Katy and the Frisco.

Appellants make no effort to show that the divisions prescribed by the Commission in this case are actually fair to the Katy and the Frisco. Instead, their position is that the prescribed divisions are fair to the Midwestern railroads as a group and that the Commission had no duty to consider the impact of divisions it prescribed upon individual railroads (U. S. Brief, pp. 26-40; C&NW Brief, pp. 78-82). Thus, under their view, it makes no difference whether the prescribed divisions are fair to the Katy and the Frisco or not.

Appellants' position is basically unsound in at least two separate respects. First, as is shown in the brief being filed by the Mountain-Pacific railroads, the Commission did not make sufficient findings to permit it to determine the fairness of the prescribed divisions as between the Midwestern railroads and the Mountain-Pacific railroads, as groups. We agree with these contentions of the Mountain-Pacific railroads and join in their position that the Commission's orders were properly set aside on this ground alone. In addition, however, we believe that even if it were assumed that the prescribed divisions were fair in the aggregate as between the contending railroad groups, those divisions could not be upheld without a determination of their fairness to the Katy and the Frisco. It is with this latter defect in the Commission's reports and orders that this brief will principally deal.

Appellants' contention that the District Court erred in setting aside the Commission's orders for failure to consider and explain their impact upon the Katy and the

Frisco rests upon the assumption that the Commission prescribed divisions for all the Midwestern railroads in line with the evidence presented by those railroads as a group and that the Katy and the Frisco were treated just like all the other Midwestern railroads. The Midwestern appellants state this assumption explicitly (C&NW Brief, pp. 85-86):

> "In the proceedings before the Commission, the Katy and the Frisco associated themselves with the Midwestern group (R. 1, 6, 8, 493). They joined with that group in presenting typical evidence demonstrating the characteristics of the traffic, revenues, economic conditions, and costs in the area served by the group. The two roads presented no evidence differentiating their individual situations from those of the other carriers in the Midwestern group. They asked for and were accorded by the Commission the same treatment given to the other Midwestern carriers."

The Government implies the same view when it attempts to brush aside the Katy's and Frisco's position as a contention that they "should have been accorded special treatment by the Commission" (U. S. Brief, p. 43).

The fact of the matter is, of course, that the Katy and Frisco are not asking, and have never asked for special treatment in these proceedings. Our complaint is that we have not received **equal** treatment, under either the evidence presented or the Commission's own findings, with the other members of the Midwestern group of railroads. As shown above, the Commission found that the Midwestern railroads were entitled to receive increases in their divisions on the basis of both cost of service and revenue need. If these findings are valid,[3] as appellants must

[3] We agree with the position taken in the brief of the Mountain-Pacific railroads that the Commission's conclusions are unlawful, both as to costs and as to revenue needs. The issues un-

assume in attempting to defend the Commission's orders, the Katy and the Frisco plainly were entitled to increases in their divisions as much as any other member of the Midwestern group. But the divisional scales actually prescribed by the Commission gave no effect to either of these findings insofar as the Katy and the Frisco were concerned. While other Midwestern railroads were being given increased divisions, we were singled out of that group and forced to bear drastic losses.

Appellants' attempt to characterize the Katy's and the Frisco's objection to this action as a plea for special treatment rests wholly upon the fact that the Commission prescribed uniform scales of divisional factors throughout the Midwest. But these scales cannot constitute a measure of the fairness of the prescribed divisions for the Katy and the Frisco, or, for that matter, for any other railroad, in view of appellants' explicit admission that such scales are not themselves related to the standards of Section 15 (6), but are "nothing more than 'a mechanical device or method for dividing the rates in the proportion warranted by the facts'" (U. S. Brief, p. 56; C&NW Brief, p. 89). The problem with the scales prescribed here is that they do **not** divide the rates in the proportion warranted by the facts in this case, as established by the Commission's own findings. These scales are based neither upon the relative costs nor the relative revenue

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derlying the cost conclusion are, of course, not before this Court since they were expressly reserved by the District Court (R. 1733). But the revenue needs issues are here, and the Mountain-Pacific railroads show, correctly we believe, that the Commission's conclusion with respect to relative revenue needs was unsupported by necessary findings and was based upon a passenger deficit theory which is irrational and unlawful. Nonetheless, the Commission's orders must be upheld, if at all, on the grounds upon which they were based. **Securities & Exchange Commission v. Chenery Corp.**, 332 U. S. 194, 196 (1948). Hence, the divisions prescribed by the Commission must be justified under the Commission's revenue needs conclusion, even though that conclusion is, we believe, itself unlawful.

needs of the two groups of railroads involved, nor can they be explained in terms of any combination of these two statutory standards. The Commission sought to explain the scales as based upon rate scales similar to those used in other cases and defended such a practice on the theory that "it is reasonable to divide the rates to some extent in accordance with the way they are made" (R. 1079). As shown in the brief of the Mountain-Pacific railroads, this practice of basing divisions upon rate scales is inconsistent with Section 15 (6) of the Interstate Commerce Act, and it has since been abandoned by the Commission itself.

But whatever the legality of the practice of patterning divisions upon rate scales in cases where it was applicable, the divisional scales prescribed here cannot be justified on any such theory, for the undisputed evidence of record in this case establishes that transcontinental rates are not made on the basis of the rate scale from which these divisional scales were made (R. 148). Thus, the scales prescribed here might as well come out of thin air. Certainly, they cannot be justified on the basis of the Commission's cost and revenue needs findings, for they produce divisions which, in many cases, give the Midwestern railroads far more than they could conceivably be entitled to under either of these standards and, in some instances, drastically decrease the Midwestern railroads' revenues without regard either to relative costs or to relative revenue needs.

The Katy and the Frisco are the principal victims of the Commission's failure to prescribe divisions which actually give effect to its findings with respect to relative costs and revenue needs. The Commission's general cost and revenue need findings are as applicable to the Katy and the Frisco as to any other Midwestern railroad, and for all that appears in the Commission's original report, it would seem that the Commission thought that it was

prescribing increases in the Katy's and Frisco's divisions in accordance with those findings. Indeed, although the Midwestern appellants seek to make it appear otherwise, there is not a single finding in either of the Commission's reports which justifies the imposition of revenue losses upon the Katy and the Frisco.[4]

The appellants themselves seem to recognize this when they turn to defend the divisional scales which the Commission prescribed, for in this part of their brief, they explicitly recognize that the Commission found that the Midwestern railroads, which of course include the Katy and the Frisco, "should have 'moderate increases' in their divisions" (C&NW Brief, p. 89; see also U. S. Brief, p. 52). Indeed, in this part of their brief, the Midwestern appellants actually treat the prescribed divisions as though they do increase the revenues of the Katy and the Frisco (C&NW Brief, pp. 89-90):

> "On the basis of its findings on relative costs the Commission determined that the existing divisions were unjust and unfair to the Midwestern lines and that they should have 'moderate increases' in their divisions (R. 1039, 1086). The Commission was entitled to exercise its discretion in selecting a mechanism that would produce the 'moderate increases' that it found were justified."
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> • • • • • • • •
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> "In the present case, the Commission found that the prescribed scales of prorating factors would give

[4] The Midwestern appellants assert that the Commission found that the Katy's and the Frisco's losses "followed principally from reductions in their existing divisions on the hauling of lumber which were high because of the desire of the Mountain-Pacific lines to maintain competitive routes via Kansas City" (C&NW Brief, p. 44). But the Commission made no finding at all with respect to the existing level of these lumber divisions. Most significantly, the Commission did not find that these or any other of Katy's and Frisco's divisions were excessive when judged by the standards of Section 15 (6).

> the Midwestern lines the 'moderate increases' to which they were entitled. There was therefore no lack of rational relationship between the Commission's findings and its choice of the scales of prorating factors because the choice of the mechanism was directly and reasonably related to an end that the Commission's antecedent findings entitled it to achieve."

This argument, in our view, conclusively demonstrates the total lack of any rational basis for the Commission's treatment of the Katy and the Frisco in this case. If the Midwestern appellants are correct and the Commission was simply looking for a convenient mechanism to give effect to findings that the Katy and the Frisco are entitled to "moderate increases," plainly it should have selected a mechanism that would accomplish that purpose. Divisional scales which impose drastic losses cannot conceivably be an appropriate mechanism directly and reasonably to the end of giving effect to findings that the Katy and the Frisco are entitled to "moderate increases."

What is really involved in this case is not a plea for special treatment by the Katy and the Frisco, but an effort on the part of the Midwestern appellants to take advantage of some wholly unjustifiable divisional scales which the Commission prescribed without regard to the standards of Section 15 (6). These scales have widely differing impacts upon different members of the Midwestern group of railroads, a fact which the Midwestern appellants conveniently ignore when they blandly assert that "the prescribed scales of prorating factors would give the Midwestern lines the 'moderate increases' to which they were entitled" (C&NW Brief, p. 89). Thus, even if the prescribed divisions do produce only "moderate increases" when the Midwestern lines are considered as a group—and we frankly admit that we do not know what the term

"moderate" means in that context—it seems plain to us that the only way that aggregate result was achieved was by giving **substantial** increases to the Midwestern appellants[5] to offset the fact that the Katy and the Frisco are forced to absorb losses under the prescribed divisions and some other Midwestern railroads would receive approximately the same divisions. The divisions which the Midwestern appellants seek to defend thus plainly represent a windfall to them under their own theory of the case.

In their briefs before this Court, appellants seek to gloss over this hard fact by a lengthy discussion of the power of the Commission to prescribe divisions on a group basis and the difficulties inherent in any other approach to the problem (U. S. Brief, pp. 26-40; C&NW Brief, pp. 78-82). But all of this discussion is plainly beside the point, for as shown above, what the Frisco and Katy are seeking is not **special** treatment but **equal** treatment under the Commission's own findings with other members of the Midwestern group of railroads. None of the divisions cases cited by appellants (U. S. Brief, pp. 29-34; C&NW Brief, pp. 79-80) remotely suggests that the Commission can deal with railroads as a group in a divisions case in a way that treats some members of the group quite differently from others. And the appellants ignore the only precedent which is really in point—namely, the opinion of Judge

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[5] As is shown in the brief of the Mountain-Pacific railroads, this is exactly what happened, for the prescribed scales have by far their greatest impact in so-called Midwest-East territory between the principal East-West gateways at Chicago, Peoria and St. Louis and the Missouri River gateways at Omaha and Kansas City. The result of this is particularly unfair to the Katy and the Frisco. Their participation as carriers between St. Louis and the Missouri River is of such small significance as to make the benefits of these substantial increases negligible, but the greater portion of the traffic in which they participate is in the area where they must absorb a part of the effect of such increases on traffic they handle west of the Missouri River in connection with the Midwest-East lines.

Doyle in **Atchison, T. & S. F. Ry. Co. v. United States,** 225 F. Supp. 584 (D. Colo. 1964). There, the court set aside a Commission order prescribing divisional scales similar to those prescribed here on the specific ground that it had not been shown that such scales treated individual carriers fairly, saying (225 F. Supp. at 595):

> "Before it relies on average or aggregate data, the Commission must make sure that the divisions formula under consideration (although seemingly just and equitable when viewed in terms of its impact on a group of railroads as a group) has not been constructed in such a way that its impact on any particular division of any particular rate as applied to any particular carrier is unjust."

The **Santa Fe** case is particularly relevant to the issue presented here, because that case, like this one, originally started as a group case, but concluded with an order that treated certain members of the group radically different from others. There, the Commission found that the prescribed divisions would increase the divisions of the Eastern railroads "by about $3 million annually" and that "[s]uch a result would be consistent with the evidence pertaining to revenue requirements of the respective groups." **Akron, C. & Y. R. Co. v. Atchison, T. & S. F. Ry. Co.,** 316 I. C. C. 351, 362 (1962). However, the divisional scales prescribed by the Commission were highly favorable to short-haul carriers, so the long-haul Eastern railroads in New England would actually have received less revenues under the prescribed scale (*ibid.*). In setting this order aside, Judge Doyle observed (225 F. Supp. at 606):

> "Since the 28277 scale principally affects those lines with shorter movements in Official territory, it would not be unreasonable to require the Commission to show some evidence of the revenue needs of these lines . . ."

The court below quoted at length from the opinion in the **Santa Fe** case and expressly relied upon the same principles in setting aside the orders here because the Commission had relied upon group evidence in prescribing divisions which benefited only part of the group, and because it had not made certain that the divisions it prescribed were fair not only in the aggregate to groups of carriers, but to each member of that group (R. 1728). This holding is clearly correct.

Section 15 (6) of the Interstate Commerce Act (49 U. S. C. § 15 (6)), which defines the responsibility of the Commission in divisions cases, plainly requires the Commission to prescribe the "just, reasonable, and equitable divisions . . . **to be received by the several carriers**" (emphasis supplied). In making this determination, the Section also directs the Commission to consider the situation of "any particular participating carrier" and any "fact or circumstance which would . . . entitle one carrier to a greater or less proportion than another carrier."[6]

In **United States v. Abilene & Southern R. Co.**, 265 U. S. 274 (1924), this Court squarely held that Section 15 (6) requires the Commission to consider the lawfulness of divisions from the standpoint of individual carriers, saying (265 U. S. at 291):

> "The power conferred by Congress on the Commission is that of determining, in respect to each joint rate, what divisions will be just. Evidence of individual rates or divisions, said to be typical of all, affords a basis for a finding as to any one. But averages are apt to be misleading. It cannot be inferred that every existing division of every joint rate is unjust as between particular carriers, because

[6] In arguing that "there is no suggestion in the text that the criteria for measuring the justness of each division of each rate pertains to particular carriers rather than to groups of carriers" (U. S. Brief, p. 35), the Government simply ignores this part of Section 15 (6).

the aggregate result of the movement of the traffic on joint rates appears to be unjust."

Appellants do not attempt to deal either with the language of Section 15 (6) or with the Court's holding in the **Abilene & Southern** case in arguing that the Commission is not required to consider the situation of individual carriers in a divisions case. Instead, they cite a group of cases arising under entirely different statutes and involving situations unrelated, for the most part,[7] to the railroad industry, in which this Court upheld some administrative regulation that was imposed on a group basis (U. S. Brief, pp. 35-36). On the strength of these cases, they argue that the impact of an administrative order upon an individual firm is irrelevant as a matter of principle so long as the order is otherwise valid (U. S. Brief, p. 36).

Whatever validity such a principle may have when applied to the situations with which the Court was dealing in those other cases, it plainly has nothing whatever to do with the proper interpretation and application of Section 15 (6). Unlike the situation which prevails in most other industries, the railroad industry cannot realistically be treated as a fungible group of firms providing competitive service in a common market. Although there is considerable competition among railroads, many cities and communities in this country are served by only one railroad. Of 416 communities served by the Frisco, for

[7] The only case cited in this connection which concerned the railroad industry is **New York v. United States**, 331 U. S. 284, 310 (1947), which involved the lawfulness of an order of the Commission removing a discrimination in class rates between various sections of the country. Since this was a discrimination proceeding, not a revenue proceeding (331 U. S. at 350), the Commission had no occasion precisely to determine the revenue needs of any of the railroads, by groups or individually. Moreover, as is explained below (pp. 25-27), rate proceedings are quite different from divisions proceedings insofar as the need for consideration of the situations of individual carriers is concerned.

example, only 209 are served by another railroad (Exhibit MW-102, pp. 4, 5), leaving 207 communities with no other railroad to look to for service. Moreover, virtually every city must depend upon a single railroad to connect it with some areas of importance to its economy. And this, too, is particularly true of the Katy and the Frisco, for both those railroads serve predominantly rural agricultural areas (Exhibit MW-102, p. 15; MW-103, p. 2) which have no other rail service by which vital crops can be transported to market. Thus, the destruction or the serious weakening of railroads like the Katy and the Frisco cannot simply be shrugged off as though some other railroad could provide the same service to their customers. If either of these railroads is destroyed, many members of the public will be wholly without needed rail service.

Because of the dependence of large segments of our population upon a single railroad, it has long been established that the Interstate Commerce Commission cannot deal with the railroads on the basis of group averages and aggregates without consideration of the impact of its orders upon individual carriers. Section 15 (6) is not the only section of the Interstate Commerce Act which requires consideration of the situation of individual railroads. Section 5 (2) of the Act (49 U. S. C. § 5 (2)), for example, dealing with applications for merger between railroads, includes a provision specifically directing the Commission to consider the effect upon the public interest of the inclusion of, or failure to include, other railroads in the territory involved in the proposed transaction (49 U. S. C. § 5 (2) (c) (2)). Under this provision, the Commission has repeatedly recognized a duty to consider the impact of mergers upon individual railroads and to condition any order approving a merger upon conditions designed to protect individual railroads affected by the merger. See e. g., **Pennsylvania Railroad Company—Merger—New York Central Railroad Company**, 327 I. C. C.

475, 526-527, 532-534 (1966), 328 I. C. C. 304, 311, 312 (1966). Indeed, in the review proceedings which followed the Commission's orders in **Penn-Central**, this Court has itself made it plain that the consideration of individual carriers in a merger case is a vital matter, for those orders were set aside because the Commission did not afford sufficient protection to affected carriers. **Baltimore & Ohio R. Co. v. United States**, ... U. S. ... (1967), 35 Law Week 4271 (decided March 27, 1967).

Similarly, in proceedings related to Section 1 (14) of the Act (49 U. S. C. § 1 (14)) involving the question of compensation to be paid for the use of cars not owned by the using carrier, the courts have held that the Commission must consider the effect of any formula prescribed upon individual carriers. Thus, in **Boston & Maine R. Co. v. United States**, 162 F. Supp. 289 (D. Mass. 1958), the Court set aside an order which prescribed a car rental formula that had been opposed by short-line railroads on the ground that the Commission had failed to give sufficient consideration to their proposal, saying (162 F. Supp. at 298):

> "In short we think the Commission erred in brushing aside a matter of such importance to so many **vital links in our transportation system** with little more than a casual wave of the hand" (emphasis supplied).[8]

The **Boston and Maine** per diem case is particularly relevant here, for there, as here, the Court was dealing with

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[8] On appeal by other parties, the Commission declined to defend its action and advised this Court of its readiness to "proceed in accordance with the terms of the remand," and the appeal was dismissed. 358 U. S. 68 (1958). However, this Court quoted the holding of the District Court with respect to the need for consideration of the situation of individual carriers and approved the remand of the case to the Commission on that basis (358 U. S. at 71-72).

an order which on its face dealt with all carriers uniformly. Thus, in setting the order aside, the court necessarily recognized that a seemingly uniform order might have a quite disparate impact upon different railroads depending upon their particular situations. And the court necessarily held that the Commission has a duty to consider the disparate impact of even a uniform order upon individual carriers so that the treatment of all carriers is actually justified by the evidence and findings of the Commission.

The only provisions of the Interstate Commerce Act affecting the overall revenue needs of the railroads which do not expressly require the Commission to consider the situation of individual carriers are those sections dealing with rates, such as Section 3 (1) of the Act (49 U. S. C. § 3 (1)), which prohibits rate discrimination, and Section 15 (1) of the Act (49 U. S. C. § 15 (1)), which authorizes the Commission to prescribe rates. These sections contain no provision directing the Commission to consider individual carriers, for the obvious reason that the rates of any railroad must be more or less the same as those of other railroads operating competitive routes. For the same reason, in all rate cases involving the general level of freight rates, the Commission has proceeded on a group basis, either dealing with all of the railroads in the country or those in one or more territorial groups, without regard to the needs of any particular railroads.

The Government argues from these general rate increase cases that the same procedures should be followed in divisions cases (U. S. Brief, pp. 31-32, note 18; p. 39, note 23). However, in doing so, it ignores the fact that the Commission's divisions-making power was given to it for the specific purpose of enabling it to go beyond the limitations inherent in a general rate case and deal with the actual revenue needs of particular railroads. Mr. Justice Brandeis expressly recognized this in his opinion for

the Court in **New England Divisions**, 261 U. S. 184, 190-191 (1923), where he outlined the history of Section 15 (6). As Justice Brandeis pointed out, Section 15 (6) was enacted as a part of the Transportation Act of 1920 which created an overall regulatory scheme "[t]o preserve for the nation substantially the whole transportation system" (261 U. S. at 189-190). The 1920 Act dealt with both the rates and the divisions of the railroads, but the two provisions were to work in basically different ways. Rates, of necessity, were to be made on a group basis, but the divisions-making power was specifically designed to permit the Commission to tailor its overall regulation to fit the needs of individual carriers (261 U. S. at 191):

> "The existence of the varying needs of the several lines and of their widely varying earning power was fully realized. It was necessary to avoid unduly burdensome rate increases and yet secure revenues adequate to satisfy the needs of the weak carriers. To accomplish this two new devices were adopted: the group system of rate making and the division of joint rates in the public interest. . . . Through the latter, the weak were to be helped by preventing needed revenue from passing to prosperous connections. Thus, by marshaling the revenues, partly through capital account, it was planned to distribute augmented earnings, largely in proportion to the carrier's needs."

The plain purpose of Section 15 (6) was thus recognized by Mr. Justice Brandeis as being to give the Commission power to deal with the revenue needs of individual carriers without disrupting existing rate groupings (261 U. S. at 191):

> "This, it was hoped, would enable the whole transportation system to be maintained, without raising unduly any rate on any line. The provision concerning divisions was, therefore, an integral part of the

machinery for distributing the funds expected to be raised by the new rate-fixing sections. It was, indeed, indispensable."

The Government seeks to create a wholly different impression of the holding of the Court in **New England Divisions** case, stressing the fact that the Court there upheld an order giving the entire group of New England carriers a uniform increase in their divisions on the basis of typical evidence and findings establishing their greater revenue needs (U. S. Brief, pp. 30-31). But that fact, far from justifying the action of the Commission here, actually further demonstrates its unsoundness. In the **New England Divisions** case, the Commission treated each of the carriers found to be entitled to increases in strict conformity with its findings; here the Katy and the Frisco have been singled out by the Commission itself for special treatment in direct conflict with its findings. Hence the situation here is entirely different from that in **New England Divisions.** To make the situations parallel, one would have to imagine a Commission order in the **New England Divisions** case which imposed drastic reductions on some of the New England lines in the very face of findings that the revenue needs of those lines were greater than those of their connections. Nothing said by this Court in the **New England Divisions** opinion in any way intimated that such an irrational and unfair order would have been upheld merely because other New England lines did benefit from the order.

In light of the history and plain purpose of Section 15 (6), the Government's contention that the group system of rate-making requires group divisions makes no sense at all. Nor is there any merit to the Government's related claim that "the Commission has consistently conducted divisions proceedings on a group basis" (U. S. Brief, p. 32, note 18). Indeed, the very cases cited by the

Government demonstrate to the contrary. Only three of the proceedings cited (**Official-Southern Divisions**, 325 I. C. C. 1 (1965); **Official-Southern Divisions**, 287 I. C. C. 497 (1953); and **Divisions of Rates, Official and Southern Territories**, 234 I. C. C. 175 (1939)), involved divisional controversies between the "four groups of carriers" set up for rate-making purposes to which the Government refers, and all three of these were between the same two of those groups. The other cases cited by the Government comprise principally proceedings involving less than all of the members of a group, or even a sub-group. In one of these cases, the Commission expressly held that individual railroads are not bound by the divisions in effect with other members of their group. **Official-Western Trunk Line Divisions**, 269 I. C. C. 765, 775 (1948). And as noted above (p. 20), in another of the cases (**Akron, C. & Y. R. Co. v. Atchison, Topeka & S. F. Ry. Co.**, 316 I. C. C. 351 (1962)), where the Commission allowed group considerations to override the rights of individual railroads under its findings, the prescribed divisions were set aside. **Atchison, T. & S. F. Ry. Co. v. United States**, 225 F. Supp. 584 (D. Colo. 1964).

There have, of course, been numerous cases in which divisions have been treated on a group basis, but, in others, the Commission has dealt only with the needs of individual railroads. The **Abilene & Southern** case, discussed above, was such a proceeding. As this Court recognized, that case involved only "the divisions of interstate joint rates on traffic interchanged, within the United States, by the Kansas City, Mexico & Orient system with thirteen carriers whose lines make direct connection with it" (265 U. S. at 279). More recently, the Commission decided a divisions case between only two railroads. See **Louisville & N. R. Co. v. Southern Railway**, 319 I. C. C. 639 (1963), upheld on judicial review *sub nom.* **Carolina & Northwestern Ry. Co. v. United States**, 234

F. Supp. 114 (W. D. N. C. 1964), **aff'd** 380 U. S. 526 (1965). And only two months ago, the Commission itself initiated an investigation into the lawfulness of divisions between the Western Pacific, the Denver and Rio Grande Western and the Burlington Railroads on passenger revenues collected from their joint operation of the California Zephyr. **Western Pacific Railroad Company Discontinuance of Trains Nos. 17 and 18 Between San Francisco, Calif., and Salt Lake City, Utah**, Finance Docket No. 24277, decided February 13, 1967.

The fact of the matter is that the Commission has decided some divisions cases which involved only controversies between groups of railroads and some which involved divisions between individual railroads. But in no case has the Commission announced or openly applied the principle urged by the appellants here that the fairness of a divisions order to individual railroads is irrelevant. The only case in which such a principle was even intimated is the **Santa Fe** case discussed above (p. 20), and the orders in that case were set aside on that very ground, among others. In other group divisions cases, the Commission has prescribed divisions which were fair to all carriers involved, either by treating all the carriers in each group on the same basis under the evidence and its findings, or by giving one or more carriers special treatment where the evidence so warranted. See, e. g., **Official-Southern Divisions**, 325 I. C. C. 1; 325 I. C. C. 449 (1965).

Although appellants seek to make it appear otherwise (U. S. Brief, pp. 29, 36-40; C&NW Brief, p. 81), there is nothing either impractical or useless in this approach. The Commission can and should see that its orders are fair to each carrier under the evidence presented to it. In the ordinary group case, where the railroads' principal reliance is upon group evidence, this will require no more

than that the Commission fashion its orders to conform to its group findings, for that would assure that each railroad received fair divisions under those findings. Plainly, such a process cannot be described as useless; it certainly would not have been useless to the New England lines in the **Santa Fe** case, nor would it be useless to the Katy and the Frisco in this case. Appellants' contention that this is impractical is based largely upon the claim that this would require separate findings for 300 railroads (U. S. Brief, p. 27; C&NW Brief, p. 79). But this is not so. We have never contended that the Commission should have made **separate** findings, even for the Katy and the Frisco. If the Commission prescribes divisions related to its findings on the statutory standards, it need make no separate findings for any railroad, unless a railroad makes a showing that it is entitled to special treatment. **New England Divisions**, 261 U. S. 184, 196-197 (1923). It is only where the Commission does not base its order upon its findings as to group costs or group revenue needs that the need for separate consideration and findings arises, and if that is impractical, the Commission always has available to it the simple alternative of relating its order to its findings.

In the final analysis, the issue in this case is whether an order prescribing divisions which cannot be justified by any of the Commission's findings under the standards of Section 15 (6) and which treats the Katy and the Frisco exactly opposite from the way in which they were entitled to be treated on the basis of the Commission's findings should be permitted to stand on the theory that it makes no difference what happens to individual railroads in a divisions case. We think that the proper resolution of this issue is clear, for the principle contended for by the appellants, which is necessary to uphold the Commission's orders in this case, is plainly contrary to the language of that section, and the controlling decisions of this Court.

The judgment of the District Court setting aside the Commission's orders should therefore be affirmed.[9]

II. The Katy and the Frisco Did Not Waive Their Right to Consideration of the Fairness of the Prescribed Divisions to Them as Individual Carriers.

Although they carefully avoid the use of the word in their briefs, both appellants seek to have this Court hold that the Katy and the Frisco somehow waived their right to consideration of the fairness of the prescribed divisions to them as individual carriers. The Government stresses the fact that the case was tried before the Commission as a group case and that "[n]ot a single carrier . . . sought to disassociate itself from the group which it originally selected by alleging and establishing the atypical nature of its operations" (U. S. Brief, pp. 27-28). The Midwestern appellants echo the same point, insisting that the Katy and the Frisco should be compelled to accept the prescribed divisions because they "presented no evidence differentiating their individual situations from those of the other carrier groups" (C&NW Brief, p. 86).

However, the fact that this was a group case in no way constitutes a waiver of the Katy's and the Frisco's right to have a determination of the fairness of any divisions prescribed to them as individual carriers. The evidence

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[9] We agree with the position taken by the Mountain-Pacific railroads that the District Court was correct in not retaining jurisdiction so as to use its equitable power possibly to give retroactive effect to the prescribed divisions if they are eventually reinstated by the Commission. Such a procedure could work to the disadvantage of the Katy and the Frisco, for it would tend to impel the Commission to seek a justification for what it originally did rather than revamping its entire order to place it upon a rational basis. We think that the Commission should be free from any such pressures. It will be time enough to consider the equitable powers of the District Court after the Commission issues a new order. **Lehigh Valley Cooperative v. United States,** 370 U. S. 76, 96 (1962).

presented to the Commission by the Midwestern group of railroads treated the Katy and the Frisco as wholly typical members of the group with the same right to increased divisions based upon cost of service and revenue needs as any other railroad. As pointed out above (p. 3), the cost evidence submitted was entirely on a group basis, and the revenue needs evidence affirmatively showed that the Katy and the Frisco were entirely typical members of the Midwestern group. The divisional scales proposed by the Midwestern group were an appropriate mechanism for giving effect to the evidence as to costs and revenue needs, at least insofar as the Katy and the Frisco are concerned, and certainly nothing in that proposal indicated a willingness on the part of the Katy and the Frisco to absorb losses in their revenues while other Midwestern railroads received increases based upon cost and revenue needs findings equally applicable to the Katy and the Frisco.

In its holding that the Katy and the Frisco had waived their right to have the fairness of the prescribed divisions considered for them as individual railroads, the Commission placed some reliance upon the fact that some of the Katy's and the Frisco's divisions would have been reduced under the Midwestern group's own proposal and under the Examiners' Recommended Report (R. 1091). Neither of these facts justifies the Commission's holding. The isolated reductions which would have resulted in a few divisions of the Katy and the Frisco under the Midwestern group's proposal were acceptable to us only because they simplified the divisional structure without substantially affecting the overall relationship between the divisions we proposed and the cost and revenue needs evidence we submitted. Our willingness to go along with this simplification certainly did not indicate an abandonment of our reliance upon the cost and revenue needs evidence. The Commission's reliance upon the fact that reductions would have resulted from the Examiners' recommendation is even

more clearly inadequate to support its holding of waiver, for the Katy and Frisco certainly never accepted that recommendation (see Exceptions of Midwestern Complainants to Recommended Report and Order, dated April 5, 1961, pp. 89-102).

If there has been any waiver here, it is on the part of the Midwestern appellants who treated the Katy and the Frisco as typical members of the Midwestern group in the proceedings before the Commission and now, for the first time before this Court, seek to make it appear that the situation of the Katy and the Frisco is basically different from that of other members of the group. In the proceedings before the Commission, no one suggested that the existing divisions of the Frisco and Katy were not entirely typical of those of the entire Midwestern group. Nor did anyone suggest that the costs and revenue needs of the Katy and the Frisco were somehow lesser than those of other Midwestern railroads. The case was tried before the Commission on the theory that all of the Midwestern railroads were entitled to increased divisions, and no suggestion was ever made that some of those railroads might get increases while others were forced to absorb decreases.

The position taken by the Katy and the Frisco in this Court is thus perfectly consistent with the position taken by those railroads before the Commission.[10] But the Mid-

[10] The Government makes the curious claim that in the District Court, the Katy and the Frisco "asserted inadequacies in the findings as to individual railroads only with respect to the Section 15 (6) efficiency criterion" (U. S. Brief, pp. 43-44). This simply is not so, as is plain from the brief submitted to that court by the Katy and the Frisco (see particularly pp. 19-30). The Government is apparently misled because the Katy and the Frisco did raise an additional issue with respect to the relative efficiency of individual railroads, which was not joined by the Mountain-Pacific railroads (R. 1334). However, the Katy and the Frisco joined in the other individual carrier issues raised (R. 1328-1329) and fully participated in the argument of those issues (R. 1582-1592). Indeed, counsel for the Katy and the Frisco did not even mention the efficiency issue in this argu-

western appellants are taking a flatly inconsistent position in seeking to justify the losses imposed upon the Katy and the Frisco on the theory that the situation of those railroads is basically different from that of the other Midwestern railroads. We agree with the Government that it ought to be left to individual railroads to show "that a particular carrier was improperly aligned in a certain group or that the group-based data was distorted in some way" (U. S. Brief, pp. 38-39). The problem here is that the Midwestern appellants, which are now seeking to disassociate themselves from the Frisco and Katy by claiming that the situation of those two railroads is atypical, never even suggested such a difference in situation to the Commission.

We think that there is a serious question as to whether the Midwestern appellants should be permitted to press a claim in this Court that was not presented to the Commission. But whatever the right of the Midwestern appellants to change their position, it is plain that the Katy and the Frisco have not waived their right to adhere to the position which they took before the Commission—namely, that they should be treated like all other Midwestern railroads. The Midwestern appellants are no more entitled to increases in their divisions than the Katy and the Frisco. And certainly, in a case where they joined in a common group with the Katy and the Frisco and relied upon evidence which included our costs and revenue needs, the Midwestern appellants are not entitled to substantial increases at the expense of the Katy and the Frisco, while we are forced to absorb drastic losses.

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ment (*ibid.*). In the District Court, the nature of the issues raised by the Katy and the Frisco was quite clearly understood, and the court passed upon those issues without objection from any party (R. 1732).

CONCLUSION.

For the foregoing reasons, as well as for the reasons set forth in the brief of appellees, the Atchison, Topeka and Santa Fe Railway Company, et al., in which these appellees join, the judgment of the District Court setting aside the Commission's orders should be affirmed.

Respectfully submitted,

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